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Corporations--Liability of Purchasing Corporation as to the Obligations of the Dissolved Vendor Corporation--Piercing the Corporate Veil

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CORPORATIONS — LIABILITY OF PURCHASING CORPORATION AS TO THE OBLIGATIONS OF THE DISSOLVED VENDOR CORPORATION — PIERCING THE CORPORATE VEIL. — *A* Corporation voluntarily dissolved after a National Labor Relations Board order to reinstate employees. *B* Corporation purchased the property of *A* Corporation, distributing stock to the stockholders of the latter in payment. *X* and *Y*, president and vice-president of *A* Corporation, personally purchased the property from *B* Corporation and formed three new corporations to carry on the same kind of business. Their directors, officers, and stockholders were practically the same as those of the old corporation. In a contempt proceeding for violation of the Labor Board order it was held, for defendants, that the dissolution of *A* Corporation was complete and the organization of the new corporation no mere continuation of it. *National Labor Relations Board v. Tupelo Garment Co.*[1]

How far may a corporation purchasing the assets of a dissolved corporation be held for the obligations of the latter? A number of issues are involved, all centering on whether the new corporation is really a new entity or a mere continuation of the old with a "new coat of paint". If a continuation, the new or purchasing corporation is liable by implication on the seller's contracts and other obligations.[2] The basic condition requisite to insulate the purchaser from liability is good faith.[3] To prove good faith, the purchasing corporation must have paid a valuable consideration,[4] which means something other than stock in the purchasing corporation[5] and which must be sufficient not to prejudice creditors of the seller.[6] Whether the directors, officers, and stockholders of the new corporation are the same as the old is another relevant inquiry. Such a situation will cast suspicion on the new corporation, although, absent other indications of fraud, duplication in personnel will not *per se* make the purchasing corporation liable.[7]

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[1] 122 F. (2d) 603 (C. C. A. 5th, 1941).

[2] Stanford Hotel Co. v. Schwind Co., 180 Cal. 348, 181 Pac. 780 (1919).

[3] 15 FLETCHER, CYCLOPEDIA OF LAW OF PRIVATE CORPORATIONS (Rev. ed. 1938) § 7125.

[4] Grinnel v. Detroit Gas Co., 112 Mich. 70, 70 N. W. 413 (1897); American Railway Express Co. v. Downing, 132 Va. 139, 111 S. E. 265 (1922).

[5] Friedenwald Co. v. Asheville Tobacco Works, 117 N. C. 544, 23 S. E. 490 (1895); Okmulgee Window Glass Co. v. Frink, 171 C. C. A. 195, 260 Fed. 159 (C. C. A. 8th, 1919). *Contra*: Swing v. Empire Lumber Co., 105 Minn. 356, 117 N. W. 467 (1908).

[6] 19 C. J. S. 1397.

[7] Anderson v. War Eagle Consol. Mining Co., 8 Idaho 789, 72 Pac. 671 (1903); Carter Coal Co. v. Clouse, 163 Ky. 337, 173 S. W. 794 (1915).

The possibility of collusion between the old and the new corporation will be investigated. A collusive transfer of assets will be a fraud upon creditors.[8] A leading Massachusetts case[9] closely analogous to the instant case held a new corporation taking over the assets of an old not liable on the predecessor's contract to hire, although admittedly the motive was to escape that existing obligation. That case has been criticised as sanctioning fraudulent use of the corporate fiction to avoid present obligations.[10] Assuming that there should be some limit on the legal incidents of corporate personality, courts disregard the theory of a separate legal entity only if it is used to perpetrate fraud.[11]

There was no need in the present case to pierce the corporate veil since there was no outward showing of fraud. True, *B* Corporation paid for the assets of *A* Corporation in stock,[12] but no point was made of this; nor was there any allegation that the purchase by *X* and *Y* from *B* Corporation was not for value. Allegations of fraud in dissolving *A* Corporation and in forming the three new corporations were unsupported by adequate evidence. The substantial identity of directors, officers, and stockholders, unsupported by evidence of fraud, does not render the purchasing corporation liable for contempt.[13]

The question remains whether the court decree enforcing the Labor Board order is such that, like a judgment,[14] it might follow the property and bind the new corporations. The cases are silent upon the point. Were such the case the decree would operate *in rem* and the theory of the corporate entity remain intact. Properly, it would seem, the decree should be enforced *in personam,* since

8 BALLANTINE, CORPORATIONS (1927) § 237.

9 Berry v. Old South Engraving Co., 283 Mass. 441, 186 N. E. 601 (1933).

10 Comments (1933) 47 HARV. L. REV. 135, (1934) 32 MICH. L. REV. 553, (1934) 18 MINN. L. REV. 559.

11 BALLANTINE, CORPORATIONS § 6; Canfield, *Scope and Limits of the Entity Theory* (1917) 17 COL. L. REV. 128, 192: "Such being the legal conception of the nature of a corporation justice requires that the principle of law which is based upon it should be firmly and consistently applied."

12 The petition averred that *B* Corporation had paid for the property of *A* Corporation in stock. The opinion of the court lacks comment upon this factor even though it is generally held that payment in stock for property of a corporation is insufficient consideration to render the purchasing corporation immune from the obligations of the vendor. 15 FLETCHER, *op. cit. supra* n. 3, at § 7127.

13 Anderson v. War Eagle Consol. Mining Co., 8 Idaho 783, 72 Pac. 671 (1903); Carter Coal Co. v. Clouse, 163 Ky. 337, 173 S. W. 794 (1915); George E. Warner Co. v. A. L. Black Coal Co., 85 W. Va. 684, 102 S. E. 672 (1920): "If the sale was fair and free from fraud, and there is no averment or showing to the contrary, the purchaser would take it [property] discharged of the debtor's obligations."

14 15 FLETCHER, *op cit. supra* n. 3, at § 7103.

the directors and stockholders of the new corporation are the same as those of the old. This, however, would necessitate piercing the corporate veil, which courts hesitate to do unless fraud appears. Therefore, that the court's failure to pass upon the question seems justified.[15]

W. H. S.

DIVORCE — COLLATERAL ATTACK BY SUBSEQUENT SPOUSE — ESTOPPEL. — *P*, inducing and aiding *D* to divorce *H*, in Tennessee, so that she might marry him, told *D* not to bother to have her attorney correct an allegation in her bill that *H* probably claimed legal residence in Massachusetts. The Tennessee court, finding *H* to be a nonresident, gave *H* notice by publication only. *H* did not appear and he never objected to the divorce decree. On the contrary he relied upon it and married another woman. *P* married *D* immediately after the divorce and lived with her for nearly seven years. He sought to annul this marriage on the ground that the divorce was invalid, first, because the Tennessee court had no jurisdiction of the subject matter, as the parties were not domiciled in that state; and second, because if *H* were domiciled in Tennessee, the divorce decree was lacking in due process for want of sufficient notice to *H*. Held, that the parties were domiciled in Tennessee, but *P* is estopped to question the validity of the notice to *H*. *Saul v. Saul*.[1]

The question as to whether a subsequent spouse of a party to a divorce may collaterally attack that divorce is one which can not be answered categorically. There is great confusion among the cases, which show a conflict in the generalities of language employed, as well as in the holdings. The answer is that the later spouse may or may not be allowed to collaterally attack the divorce depending on many varied circumstances. One observation worthy of note is the fact that in former cases no distinction had been drawn between cases involving lack of jurisdiction over the subject matter of the divorce, as when neither party has established a domicil in the divorce forum, and cases involving lack of jurisdiction over the person of the nonresident defendant. Total lack of power in a court to deal with the subject matter of a suit goes

[15] *Cf.* Southport Petroleum Co. v. N. L. R. B., 62 S. Ct. 452, 86 L. Ed. 397 (U. S. 1942).

[1] 122 F. (2d) 64 (App. D. C. 1941).